



Corporate Excise DOR Directive 95-10

Massachusetts
Department of
Revenue

Recapture Adjustment for LIFO Method C Corporations Converting to S Corporation Status.

Issue:

When is the LIFO recapture adjustment included in federal gross income under I.R.C. § 1363(d) reported and taxed for Massachusetts purposes?

Directive:

LIFO method C corporations converting to S corporation status must make a LIFO recapture adjustment in accordance with I.R.C. § 1363(d). The adjustment to income is made in the last taxable C corporation year before the first taxable year in which an S election is effective. I.R.C. § 1363(d)(1). Any resulting Massachusetts tax liability must be paid on or before the due date for filing the return for the last taxable year operated as a C corporation, determined without regard to any extensions of time for filing. The Massachusetts tax payments may not be spread over a four-year period as provided for federal purposes under I.R.C. § 1363(d)(2).

Discussion of Law:

Massachusetts C corporations and S corporations determine taxable income for Massachusetts tax purposes by referring to their federal gross income for the taxable year. M.G.L. c. 63, §§ 30 (C corporations) & 32D (S corporations). Federal gross income

includes income recognized under I.R.C. § 1363(d) as a LIFO recapture adjustment. This adjustment is required for LIFO method C corporations that convert to S corporation status to reflect a change in the way inventory is valued. The adjustment to income is made in the last taxable C corporation year before the first taxable year in which an S election is effective. Accordingly, Massachusetts gross income will reflect the same adjustment.

I.R.C. § 1363(d)(2) provides relief from the resulting federal tax liability by spreading the tax payments attributable to the LIFO recapture adjustment over a four-year period. Massachusetts has no corresponding provision for spreading the state tax liability. Thus, although there is federal tax payment relief under I.R.C. § 1363(d)(2), the taxpayer must pay the entire amount of Massachusetts tax attributable to the LIFO recapture adjustment with the filing of the last C corporation return.

Mitchell Adams
Commissioner of Revenue
September 27, 1995

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